

Jul-22-04

10:29am From-SHIU YIP - KKR

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KOHLBERG KRAVIS ROBERTS & CO.

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JUL 27 2004

Federal Communications Commission
Office of the Secretary

July 22, 2004

Sent Via FedEx

The Honorable Michael K. Powell
Chairman
Federal Communications Commission
445 12th Street, S.W.
Washington, D.C. 20554

Re: CC Docket 98-96; Potential Interim Rate Increases for DS-1 loops and transport

Dear Chairman Powell:

As the largest investor in NuVox Communications (NuVox),* the private equity firm of Kohlberg Kravis Roberts & Co. L.P. has substantial interest in the future regulation of access to ILECs' bottleneck facilities and the availability and pricing of DS-1 loops and Enhanced Extended Loops (EELs) in particular. As such, I am writing to express our deep concern with certain aspects of potential interim UNE rules under consideration by the Commission, specifically, the automatic rate increases for DS-1 loops and EELs pending adoption of permanent rules. Such a ruling could have disastrous consequences for facilities-based CLECs and the small businesses that have come to rely upon them to offer affordable access to innovative new telecommunications service offerings.

Instead of pursuing the proposed interim order, we respectfully ask that you issue an order preserving the status quo for six months with new permanent rules issued within that timeframe, and that, to preserve facilities-based competition, you refrain from prescribing automatic price increases for DS-1 loops and EELs pending adoption of those permanent rules.

As you know, the major incumbent carriers have largely ignored small business customers, and it is the facilities-based competition that has enabled these businesses for the first time to reap the benefits of new communications technologies provided affordably by companies such as NuVox. Until now, you had championed this competition. Indeed, as you noted in your statement initiating the Triennial Review, the commitment to facilities-based competition includes "competition from newer entrants who supplement their own facilities with network elements leased from the incumbent. . . I fully support the use of facilities and individual UNEs as means to promote local competition while simultaneously furthering the related goals of encouraging deregulation and innovation."

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* For your information, the new NuVox is the result of a recent merger of its parent company with that of NewSouth Communications, combining two regional facilities-based CLECs that serve numerous markets in the Southeast and Midwest over a mix of their own network facilities and loop/transport facilities leased from Incumbent Local Exchange Carriers (ILECs) as Unbundled Network Elements (UNEs). NuVox has used the capital we and its other investors, including Wachovia Capital Partners, M/C Venture Partners, Goldman Sachs, JP Morgan, Quadrangle Group Capital Partners, Whitney & Company, and Columbia Capital, have committed to purchase and deploy network equipment and facilities to provide small and medium-size businesses in these markets with affordable access to innovative new service offerings, including broadband services.

Following through with the commitment you expressed, you joined with all of the Commissioners in unanimously adopting provisions that ensured continued access to DS1 loops and EELs. The reason was clear -- competing carriers simply cannot provide services to small business customers without access to these UNEs. With such access, facilities-based competition will continue to thrive, bringing the benefits which you so succinctly identified in your separate statement adopting the Triennial Review Order: service offerings *"differentiated from the incumbent"*; the *"real potential for lower prices"*; *"less dependency on the incumbent thereby reducing the need for regulation"*; and, the *"creation of vital redundant networks that serve our nation if other facilities are damaged by those hostile to our way of life."*

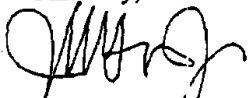
Therefore, I write to express my concern that you appear poised to turn your back on facilities-based carriers by seeking to implement interim rules that would permit the ILECs to automatically begin charging facilities-based CLECs higher rates (including full special access charges) for loop/transport facilities after the "standstill" period, potentially without any further determination of impairment. Despite the unsubstantiated assertions of the RBOCs, special access services are not an adequate substitute for cost-based UNEs, and we have become very concerned that:

- *Implementation could have very serious financial consequences:* A recent analysis shows that replacement of cost-based DS1 and DS3 loop and transport UNEs with special access services would result in a doubling or tripling (depending upon location) of the critical transmission costs incurred by UNE-L based CLECs.
- *Price increases would be passed on to the consumer:* Operating on thin margins in highly price sensitive markets, many companies would be unable to absorb such dramatic cost increases or would have no choice but to pass them along to customers in the form of increased rates.
- *Price increases could cause a serious reduction in credit:* Credit arrangements extended to CLECs typically tie their ability to draw down funds on the achievement of pre-set performance targets, and failure to achieve these targets could result in immediate cancellation of the facility, discontinuance of access to credit lines, and even a demand for immediate repayment of the previously borrowed amount -- a ruinous situation for any business. For example, a requirement that special access services be ordered for new customers would shut off new sales and cause some CLECs to violate gross revenues and sales covenants. Similarly, an across-the-board 15% increase in the price of the embedded base of high capacity loop and transport UNEs likely would cause some CLECs to violate covenants requiring them to achieve certain levels of gross margins and EBITDA. Any change in the pricing of commercial DS1 level UNEs (for which there is virtually no record evidence of non-impairment) would be particularly harmful.

Our investment in NuVox was in significant part predicated on the strong commitment to facilities-based competition expressed by you and your fellow Commissioners and on a belief that the Telecommunications Act and the Commission's rules guaranteed new facilities-based entrants access to cost-based UNEs until impairment is eradicated. While we understood the many business risks of investing in this sector, we -- as well as several other interested parties who we know have reached out to you -- had no reason to expect that there was a real risk of the government simply deciding not to implement some of the fundamental elements of the Telecommunications Act. A decision to raise DS1 loop and EEL prices to special access levels would be tantamount to a decision to no longer support facilities based competition in the telecommunications space.

We believe that the appeals court sent the FCC's rules back for modification, not to be jettisoned, and that the proper action for the FCC to take is to tweak the rules as necessary to address the court's concern, while in the interim preserving the kind of network sharing that is required in a period of transition to unbridled competition in telecommunications.

Sincerely,



James H. Greene, Jr.
Member

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